New Home Sales

(Seasonally Adjusted Annual Rates, in Thousands)

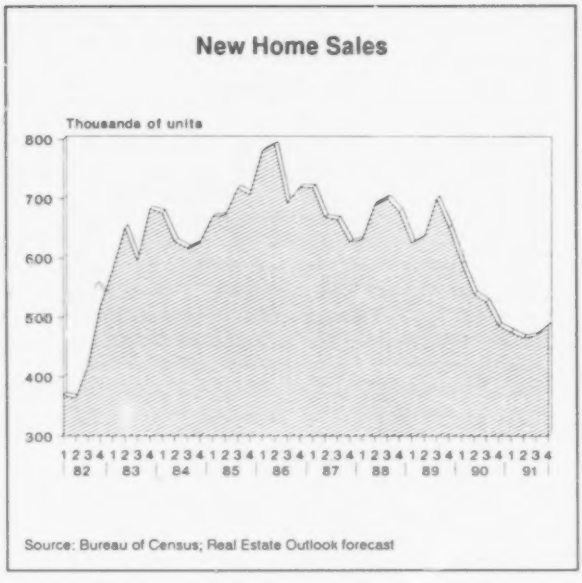
National Data

		Mo. Ago % Chg.	Yr. Ago % Chg.
Oct 1989	636	-0.3	-11.4
Nov 1989	687	8.0	5.7
Dec 1989	633	-7.9	-5.4
Jan 1990	613	-3.2	-12.9
Feb 1990	606	-1.1	-2.7
Mar 1990	558	-7.9	0.4
Apr 1990	533	-4.5	-12.6
May 1990	536	0.6	-17.7
Jun 1990	550	2.6	-14.9
Jul 1990	541	-1.6	-27.0
Aug 1990	530	-2.0	-26.3
Sep 1990	509	-4.0	-20.2
Oct 1990	***491***	**-3.5**	**-22.8**
Annual Averages:			
1988	676		0.8
1989	654		-3.3

Regional Data

	Northeast	Midwest	South	West
Oct 1989	88	101	271	176
Apr 1990	86	90	209	148
May 1990	71	91	215	159
Jun 1990	80	94	233	143
Jul 1990	70	93	238	140
Aug 1990	61	91	238	139
Sep 1990	57	94	221	137
Oct 1990	***84***	***83***	***212***	***112***
Annual Averages:				
1988	101	98	271	206
1989	90	103	258	202
Percent Changes in October 1990 since:				
Oct 1989	-4.5	-17.8	-21.8	-36.4
Sep 1990	47.4	-11.7	-4.1	-18.2

Source: Bureau of Census, Construction Reports, Series C25



Source: Bureau of Census; Real Estate Outlook forecast

Source: Bureau of Census

The new homes sales rate dipped below the half-million mark in October, when the annual pace fell 3.5 percent to 491,000 units. October also marks the fourth consecutive monthly decline and the ninth month in the past twelve that the sales rate has fallen. The rate is almost one-quarter below last October's sales rate.

The Northeast had a surprisingly strong October, according to the preliminary data. The sales rate jumped to 84,000 units, almost 50 percent higher than September's 57,000 unit rate. While the month was the strongest in the region since April, it remained 4.5 percent below the rate set in October 1989. The remaining three regions experienced declines in October, with the sharpest being an 18.2 percent decline in the West. The Midwest was off by 11.7 percent, and the South fell by 4.1 percent.

Sales of new homes are expected to average 487,000 in the final quarter of 1990, down 7.6 percent from the third quarter. With housing starts expected to continue its descent during the recession, sales of new homes will also be falling. The bottom will be reached in the second quarter of 1991, when the sales rate is expected to reach 466,000 units. The recession will send mortgage rates down and, by the second half of 1991, the economic recovery will foster an increase in demand for new homes. It is possible that the buying opportunities afforded by lower mortgage rates and rising incomes in late 1991 and into 1992 may catch home builders short of supply.

Existing Single-Family Home Sales

(Seasonally Adjusted Annual Rates, in Thousands)

National Data

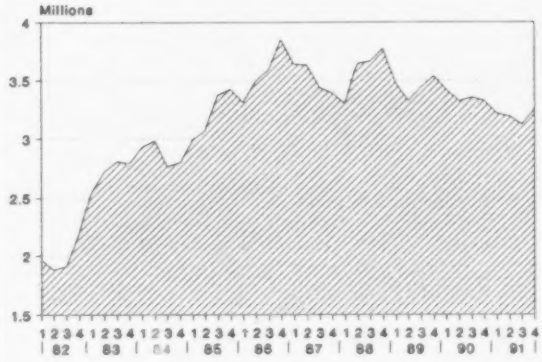
		Mo. Ago % Chg.	Yr. Ago % Chg.
Oct 1989	3,490	-0.6	-5.2
Nov 1989	3,560	2.0	-4.0
Dec 1989	3,560	0.0	-9.2
Jan 1990	3,470	-2.5	-5.2
Feb 1990	3,400	-2.0	-4.2
Mar 1990	3,400	0.0	-0.9
Apr 1990	3,330	-2.1	-3.2
May 1990	3,300	-0.9	1.5
Jun 1990	3,330	0.9	0.0
Jul 1990	3,330	0.0	-1.5
Aug 1990	3,500	5.1	1.7
Sep 1990	3,170	-9.4	-9.7
Oct 1990	***3,020***	***-4.7***	***-13.5***
Annual Averages:			
1988	3,594		-1.9
1989	3,467		-3.6

Regional Data

	Northeast	Midwest	South	West
Oct 1989	610	970	1,300	610
May 1990	520	880	1,320	570
Jun 1990	490	960	1,310	580
Jul 1990	560	930	1,310	530
Aug 1990	520	990	1,400	570
Sep 1990	520	870	1,260	520
Oct 1990	***470***	***820***	***1,230***	***490***
Annual Averages:				
1988	669	929	1,348	643
1989	590	931	1,320	617
Percent changes in October 1990 since:				
Oct 1989	-23.0	-15.5	-5.4	-19.7
Sep 1990	-9.6	-5.7	-2.4	-5.8

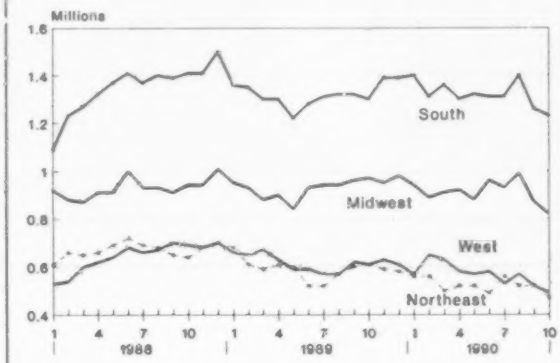
Source: National Association of Realtors,® "Home Sales"

Existing Home Sales



Source: NAR Economics & Research; Real Estate Outlook forecast

Existing Home Sales by Region



Source: NAR Economics & Research

The deteriorating economy caused existing home sales to decline 4.7 percent to their lowest level in nearly six years. In the two months since posting a sizable gain in August, sales dropped by a cumulative 13.7 percent to stand at an annual rate of 3,020,000 units.

On a year-to-date basis, sales have slipped 3.6 percent in 1990 relative to 1989. The declines have been the most severe in the Northeast and the West, which are off 11.7 percent and 7.6 percent, respectively, in the year's first ten months. The Midwest has dropped 1.4 percent, and the South's sales pace has risen 1.1 percent.

The more recent performance is more ominous, however, suggesting that the declines on the coasts have spread to the rest of the nation. In contrast to modest gain noted above so far in 1990, the sales pace in the South fell 12.1 percent from August to October. The Midwest has experienced the sharpest fall, 17.2 percent, over the two months. The West dropped 14 percent and the Northeast slipped 9.6 percent. These declines correspond, of course, with the sharply increased fear of recession that came in the wake of the eruption of the Persian Gulf crisis.

The fourth quarter of 1990 is expected to be the low point for existing home sales, with marginal improvements made in the following two quarters. The rebound in the economy and lower interest rates will push existing home sales up in the last half of 1991. Sales are projected to be down 3.0 percent in 1991 but up 7.2 percent in 1992.

Single-Family Home Prices

(In Dollars)

National Data

	Median		Average	
	Existing	New	Existing	New
Oct 1989	92,400	123,000	116,700	147,800
May 1990	95,600	125,000	118,700	150,600
Jun 1990	97,500	125,000	121,100	150,400
Jul 1990	98,300	118,700	122,000	149,800
Aug 1990	97,100	118,500	120,500	145,300
Sep 1990	94,400	112,900	116,700	143,400
Oct 1990	***92,800***	***121,800***	***115,700***	***157,500***
Annual Averages:				
1988	89,200	113,400	112,500	138,900
1989	92,900	120,400	118,000	148,300
Percent changes in October 1990 since:				
Oct 1989	0.4	-1.0	-0.9	6.6
Sep 1990	-1.7	7.9	-0.9	9.8

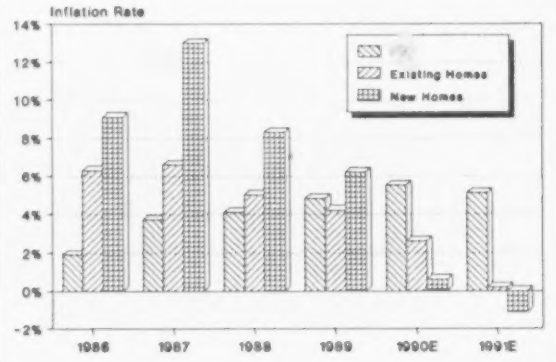
Regional Data

Median Prices for Existing Single-Family Homes

	Northeast	Midwest	South	West
Oct 1989	143,200	71,600	83,600	140,300
May 1990	141,300	73,500	85,100	141,800
Jun 1990	148,300	75,900	87,500	138,100
Jul 1990	146,900	76,000	88,800	139,700
Aug 1990	145,300	75,300	86,900	140,200
Sep 1990	137,100	74,200	85,900	134,700
Oct 1990	***136,200***	***72,100***	***83,400***	***140,600***
Annual Averages:				
1988	142,500	68,200	82,200	124,700
1989	145,100	71,200	84,400	139,800
Percent changes in October 1990 since:				
Oct 1989	-4.9	0.7	-0.2	0.2
Sep 1990	-0.7	-2.8	-2.9	4.4

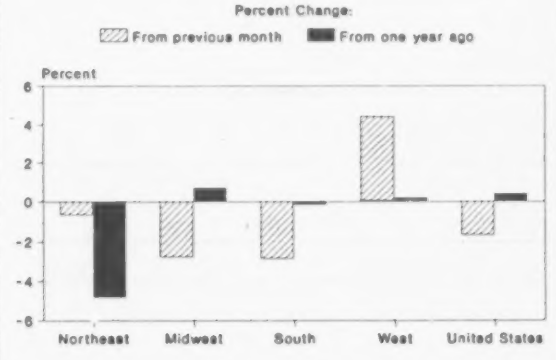
Source: National Association of Realtors,® "Home Sales"

Home Prices



Source: Bureau of Census; E Real Estate Outlook forecast

Home Prices by Region



Source: NAR Economics & Research; Real Estate Outlook forecast

Median prices of existing homes fell by 1.7 percent in October to $92,800, $1,600 below September's level. Although the October figure is about 6 percent below July's peak, it remains higher than the median price in October 1989. The median price for new homes, on the other hand, jumped $8,900, or 7.9 percent, in October to stand at $121,800. The rebound comes after the median price for new homes had dropped $12,100, or 9.7 percent, between June and September. Relative to its level of a year ago, the median price is down by 1.0 percent.

The higher prices for new homes is also reflected in measures of average prices. In October, the average new home price gained $14,100, or 9.8 percent, to stand at $157,500. Given the market conditions and the sluggishness of the new homes market (see page 5), this suggests that the composition of new homes sold may have shifted to more expensive homes rather than price increases on individual homes.

The unequal regional difficulties in housing markets is reflected in the median prices for existing homes. Relative to October 1989, prices in the Midwest, the South and the West show basically no change, but prices in the Northeast have dropped 4.9 percent.

Robert D. Barr
Director of Forecasting
Forecasting & Policy Analysis Division

THE 1991 BUDGET AND HOUSING BILL: A RENEWED COMMITMENT

Congress and the Administration have shaken hands, albeit reluctantly, on a long-awaited budget resolution. The final Omnibus Budget Reconciliation Act of 1990, which is a hodgepodge of spending cuts, revenue enhancements, program reforms and rules for greater oversight, is designed to slice $500 billion from the burgeoning federal budget deficit over a five-year period, and $40 billion in 1991 alone.

Getting there wasn't easy though -- the road to the budget agreement was a long and winding one. The journey began on January 29 when President Bush submitted his $1.23 trillion spending plan to Congress. Negotiations between Congress and the Administration formally began on May 9. And it was in early November when major newspapers across the country heralded the arrival of a budget agreement.

The 1991 Budget agreement and housing legislation is, in many respects, a renewal of federal commitment to housing. This federal commitment to housing flows through two primary channels: 1) increased funding for existing programs and new programs under the Cranston-Gonzalez National Affordable Housing Act, and 2) extensions of several of the tax incentive programs. This article looks at the National Affordable Housing Act then turns to the tax incentive programs for housing.

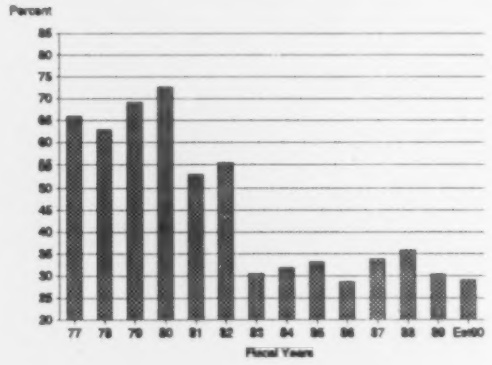
NATIONAL AFFORDABLE HOUSING ACT

President Bush recently signed a two-year $57.4 billion housing bill. The bill provides funding for some of the existing housing assistance programs, includes measures to aid the financially faltering Federal Housing Administration, and funds some of U.S. Department of Housing and Urban Development (HUD) Secretary Jack Kemp's HOPE proposals. Funding within the housing bill includes increases of $273 million for Community Development Grants; $1.8 billion for assisted housing; $6.7 billion for renewal of expiring federal contracts; and $235 million for operating subsidies for low-income housing.

Table 1 shows that from 1977 to 1982, rental commitments through production programs -- which include Section 8 new construction and substantial rehabilitation, public housing, and Farmers Home Administration Section 515 programs -- ranged from 53 percent to 73 percent of all new rental commitments. Since 1982, additional rental commitments for these programs have been only about one-third of the total.

Net new rental commitments are the number of housing units for which funds are appropriated in a given year. This does not necessarily mean that the units are constructed within the appropriation year, only that the money to do so has been committed. These numbers take into account units for which funds are deobligated or cancelled that year, as well as units replacing those lost because private owners of assisted housing opted out of programs or because public housing units were demolished.

Table 1
NET NEW FEDERAL COMMITMENTS FOR RENTERS THROUGH NEW PRODUCTION
(as percent of total net new commitments for renters)



SOURCE: Congressional Budget Office based on data provided by the HUD and Farmers Home Administration.

In an important change of policy, the legislation resumes federal support for new production of affordable housing. Local and state governments may now use a $3.1 billion line of credit provided by HUD on a range of housing projects including housing rehabilitation, new construction, and tenant acquisition of public units.

Federal Housing Administration (FHA) and Secondary Mortgage Markets

For mortgage programs, Congress authorized a $76.8 billion limit on Federal Housing Administration (FHA)-insured mortgages for fiscal year (FY) 1991 (and $79.8 billion for FY 1992.) To date, actual appropriations for FY 1991 are $75 billion, an increase of $8.0 billion over the 1990 appropriation.

Congress also authorized an $84.9 billion ceiling on Government National Mortgage Association (GNMA)-guaranteed mortgage-backed securities for FY 1991 (and $88.3 billion for FY 1992.) To date, actual appropriations for FY 1991 are $80 billion -- representing an increase of $5.0 billion over the 1990 appropriation.

A 1989 appropriations bill temporarily raised the ceiling on the FHA loan amount for high-cost areas from 150 percent to 185 percent of the base limit of $67,500 ($101,250 to $124,875). The National Affordable Housing Act establishes the $124,875 ceiling until further modifications.

The changes to the FHA mortgage insurance program increase the equity stake required of FHA home buyers to reduce risk to the Mutual Mortgage Insurance (MMI) Fund. This new legislation generally increases the upfront costs which must be borne by homeowners by restricting the allowed FHA loan amount (before mortgage insurance premium). The mortgage may not involve a principal obligation in excess of 98.75 percent of the appraised value of the property (97.75 percent, in the case of a mortgage on a property with an appraised value in excess of $50,000), plus the amount of the mortgage insurance premium paid at the time the mortgage is insured.

Home buyers are required to pay a risk-based premium of 0.5 percent of their loan balance for a specified number of years depending on the loan-to-value (LTV). That is, home buyers who can lower their LTVs by making larger down payments will pay the premium for a shorter period.

Under these changes, the government is expected to save approximately $3.4 billion over five years. However, as noted earlier, these changes will increase the cost of using FHA-mortgages. For a typical FHA-insured home of $65,000, home buyers will have to put up approximately $564 more. The Center on Budget and Policy Priorities reports in its November publication, One Step Forward, that between 35,000 and 100,000 fewer households will be able to participate in FHA-insured mortgages each year due to the changes.

National Homeownership Trust Demonstration (NHT)

The housing legislation established a National Homeownership Trust Demonstration designed to provide assistance to first-time home buyers. Congress has authorized $250 million for FY 1991 and $521.5 million for FY 1992.

To qualify for this assistance, the home buyer's income for the previous year cannot exceed 95 percent of the median area income for a family of four, or 115 percent of median area income in designated FHA high-cost mortgage areas. These limits will be adjusted for family size. The property must be a single-family residence or co-op unit that is intended as the buyer's principal residence and the mortgage amount cannot exceed the FHA limit.

NHT assists first-time home buyers in two ways. First, NHT can buydown the effective mortgage rate such that it does not exceed six percent. Second, NHT can assist with down payment and closing costs, provided that the home buyer pays at least one percent of the cost of acquisition (excluding any upfront mortgage insurance premium). NHT funding is secured by a lien on the property.

Recipients of NHT assistance must continue to meet the conditions of the program or NHT can request the repayment of assistance. An example of a condition under which NHT can request repayment is an appreciable increase in the recipient's income for a sustained period of time. That is, if family income exceeds the program limit for a two-year period, then NHT can request repayment, even if the family is still living in the home.

Homeownership and Opportunity for People Everywhere (HOPE) and HOME Investment Partnerships Act Programs

The programs of HOPE and HOME are designed to promote the expansion of housing opportunities to low- and moderate-income households. While the purpose of HOPE is primarily to encourage homeownership among such households, HOME is designed to increase investment in affordable rental housing, primarily through the rehabilitation of existing structures.

To these ends, $1 billion has been authorized for HOPE programs over two years.

The three categories of homeownership programs are HOPE for Public and Indian Housing Homeownership; HOPE for Homeownership of Multifamily Units; HOPE for Homeownership of Single Family Homes. While the specifics of the three categories of programs differ, the bottom line is the same -- the encouragement of homeownership among low-income families.

The essential elements for public and Indian housing include the following. HUD will grant money to certain entities, such as non-profit organizations and resident management corporations, for tenants of public and Indian housing to acquire ownership of their homes. The tenants must acquire ownership interest in at least one-half of the project units, and the purchase price cannot exceed 30 percent of the tenant's adjusted monthly income. Twenty-five percent of HUD assistance must be matched by nonfederal sources.

In return for the assistance, the proceeds from sale which the recipient can retain are limited. If the property is sold within the first six years, the amount received by the homeowner will be limited to the homeowner's initial contribution, value of any improvements paid by the seller and an inflation adjustment. For resales between six and twenty years, HUD or the homeownership program will recapture the difference between the initial purchase price and the market value at the time of purchase. Stated otherwise, HUD will recapture the assistance. The sale proceeds which are not retained by the seller are split 50-50 between HUD and the organization that originally sold the units to the seller.

The elements of HOPE programs for multifamily and single-family units are similar to that of public and Indian housing. The only major differences are higher matching requirements for both multifamily and single-family (33 percent for both types compared to 25 percent for public and Indian housing), and greater ownership interest required (100 percent for multifamily versus 50 percent for public and Indian housing.)

HOME received funding of $1 billion for FY 1991 and $2.1 billion for FY 1992. Sixty percent of these funds will go to local governments and 40 percent will go to the states, with a minimum allocation for a state at $3 million and $500,000 for a locality. At least 90 percent of funding must be allocated to units occupied by persons with incomes at or below 60 percent of the area's median income; the remainder, if any, can serve the needs of families with somewhat higher incomes, but the incomes must be at or below 80 percent of the area's median income.

HUD will make HOME funds available to participating jurisdictions through the establishment of HOME Trust Funds. Jurisdictions in turn can make HOME funds available to private parties or government agencies in the form of equity investments, and interest-bearing or non-interest-bearing loans.

HOME funds can be used for acquisition, construction, reconstruction, and rehabilitation of affordable rental and ownership housing, with preference given for rehabilitation. If, however, the participating jurisdiction determines that rehab is not the most cost-effective way to meet the housing needs; if there is an inadequate supply of housing with rents below Section 8 Fair Market Rents; or if there is a shortage of substandard housing suitable for rehabilitation, this preference will be waived.

Each participating jurisdiction must contribute an amount equal to at least 25 percent of HOME funds used for rental assistance and rehab, 33 percent of funds for substantial rehabilitation, and 50 percent of funds for new construction. This matching assistance may be in the form of cash, land, or other in-kind contributions.

Low-Income Housing Preservation and Resident Homeownership Act of 1990

The Emergency Low-Income Housing Preservation Act of 1987 was a stop-gap measure enacted by Congress to halt the loss of affordable housing. Rewritten and renamed, the Low-Income Housing Preservation and Resident Homeownership Act of 1990 provides a more lasting solution by offering fair market incentives to owners. The Act provides owners with fair market value incentives to retain the project as low-income housing or fair market price to sell the project to a buyer willing to maintain it as low-income housing. The owner would be permitted to prepay the mortgage under restrictive conditions, including the inability to find a willing and able buyer.

U.S. Department of Veterans Affairs Loan Guaranty Program

While not technically part of the National Affordable Housing Act, alterations to the VA home loan-guaranty program affect potential

home buyers and, as such, deserve mention here. The funding fee for borrowers acquiring mortgages guaranteed by the Department of Veterans Affairs will be raised by 0.625 percentage points (1.25 to 1.875). This is slightly higher than the 0.50 percentage point increase originally proposed by President Bush. The funding fee is used to offset program operating costs, including default payments which have been particularly high in recent years. Borrowers may finance the fee as part of their mortgages, making the mortgage payment up to $2.00 a month higher.

The budget maintains the "sliding scale" adjustment for borrowers making down payments of five percent or more. VA-borrowers who make down payments of five percent to slightly less than 10 percent will now pay a 1.375 percent fee, while those making down payments of 10 percent or greater will pay 1.125 percent. Borrowers who refinance loans also pay the 1.875 percent funding fee regardless of the amount of equity in their properties. The fee increases are expected to add $79 million to the federal government's coffer over the next five years.

TAX INCENTIVES FOR HOUSING

Along with the federal housing programs contained in the National Affordable Housing Act, tax incentives also have a substantial impact on such housing activities as the construction of affordable housing and the investment in housing through homeownership.

Low-Income Housing Tax Credit

The budget extends, through 1991, the low-income housing tax credit. This tax incentive encourages private sector construction and rehabilitation of housing affordable to the working poor and other low-income families. The Joint Committee on Taxation estimates the cost of extending the low-income housing tax credit through December 31, 1991 to be around $200 million.

Under the budget, the credit allocation authority for each state in 1991 is set at a level of $1.25 per resident. And the new budget bill requires that 10 percent of the state's annual tax credit authority be set aside for projects involving qualified non-profit organizations. The law also clarifies that states are allowed to "carry over", for use in the following year, any unused tax credit authority and returned credits from the current calendar year.

Expenditures eligible for the credit remain substantially unaltered. They include the depreciable costs of new construction and substantial rehabilitation and the acquisition costs of certain buildings neither placed in service nor substantially rehabilitated during the prior 10 years.

In return for the credit, the building owner must continue to operate the project as low-income housing over an initial 15-year compliance period. An extended use period, established in 1989, is an additional period of no less than 15 years over which the owner must continue to maintain the project as low-cost. This extended use period can be terminated under select conditions. By law, an owner wanting to convert or sell a low-income building after the initial 15 years must first give the state housing credit agency one year to find a qualified buyer willing to purchase the low-income units for a restricted sales price and to maintain them as low-income rentals for the remainder of the extended use period. In the event that no buyer can be found, the owner is free to convert or sell to anyone at any price, thereby ending the extended use period.[1] In the event of a sale or conversion, the current owner may not evict any current occupants of low-income units without good cause nor increase the gross rents for their units for three years, except under select conditions. (Gross rent is contract rent plus a utility allowance. If the owner pays utilities, then the utility allowance is $0.)

The program's link between rents and area median income constitutes the basis for one such condition. An owner receiving the credit is required to reserve either 20 percent of units in his project for families earning at or below 50 percent of the area median income or 40 percent of units for families earning at or below 60 percent of the area median income. For units reserved for families earning at or below 50 percent of the area median income, the maximum rent that the owner is allowed to charge is 30 percent of 50 percent of the area median income. If the area median income is $25,000, then the owner is allowed to charge $3,750 a year ($25,000 x .5 x .3) or $312.50 a month.

If inflation pushes the area median income to $30,000, then the maximum amount an owner is allowed to charge on units occupied by tenants earning at or below 50 percent of the area median increases to $4,500 a year ($30,000 x .5 x .3), or $375 a month. (Rents for units reserved

for families earning at or below 60 percent of the area median income are similarly calculated.)

Mortgage Revenue Bond Program

Mortgage revenue bond (MRB) programs administered through State Housing Finance Agencies and local agencies have been important sources in financing home purchases to first-time buyers. The savings to investors in MRBs, which derive from tax-exempt interest earnings on the bonds, can be passed forward to mortgage borrowers in the form of below-market interest rates. It is estimated that state and local housing agencies assisted several hundred thousand first-time home buyers through the more than $50 billion in tax-exempt qualified mortgage bonds they issued between 1982 and 1986. The budget extends the authority of states (and localities) to issue MRBs through 1991. The Joint Committee on Taxation estimates the 1991-1995 cumulative cost of extending this program through December 31, 1991 to be $400 million, or roughly $800,000 a year.

The new budget maintains the limit on tax-exempt financing for private activities, including financing home purchases and multifamily construction, established by the Tax Reform Act of 1986. Each state's "unified volume cap" remains at the greater of $50 per resident of the state or $150 million.

The most significant change to the MRB program affects the recapture rules. The rationale behind the recapture requirements is that households buying homes with bond-financed mortgages should repay a portion of the subsidy if they resell their homes within a certain period and their income has risen appreciably.

Under the original recapture rules, the amount of the recapture tax increased gradually until the end of the fifth year and then declined until the end of the tenth year, when the tax fell to zero.

The new law reduces the maximum recapture period from ten to nine years, adjusts the recapture amount annually rather than monthly, and liberalizes the rules exempting homeowners with inconsequential income increases from recapture.

The recapture amount is equal to the lesser of (1) 50 percent of the gain from the disposition of the home; or (2) the product of the applicable "holding period" percentage, the imputed mortgage bond subsidy (6.25 percent of the highest principal loan balance) and an income percentage. (The specification of the highest principal loan balance as opposed to just the initial principal loan balance is necessary because there is no provision in the MRB program which prohibits negative amortization of the principal balance.)

The holding period percentage is designed to decrease the recapture tax for households remaining in their homes for longer periods. The percentages are as follows:

	Holding Period Percentage					
	0%	20%	40%	60%	80%	100%
Year of Property Dis-position	10	9	8	7	6	5

The purpose of the "income percentage," whose calculation is complicated and will not be discussed here, is to assess whether a recipient of a bond-finance mortgage has had a substantial increase in income between the year of loan origination and the year of the property disposition. The smaller the increase in income, the lower the "income percentage" and therefore the lower the recapture tax.

Mortgage Interest Deduction

The new budget maintains the principal amount on which taxpayers may deduct mortgage interest at $1,100,000 but limits the total itemized deductions which high-income taxpayers are allowed to take. Under the new budget, allowable tax deductions will be reduced by three percent, or $300, for every $10,000 of adjusted gross income in excess of $100,000 for single and joint filers and $50,000 for married taxpayers filing separately. In no event, however, may more than 80 percent of the otherwise allowable deductions be disallowed. The income thresholds will be adjusted for inflation beginning in 1991.

While mortgage interest is one of the largest exemptions that many itemizing taxpayers claim, it is important to note that taxpayers claiming the mortgage interest deduction are not "penalized" relative to other taxpayers with the same income but who do not claim the mortgage interest deduction. The reason is that the amount of deductions disallowed does not increase for higher amounts or different types of itemized deductions. The disallowed amount depends only on income. The example in Table 2 illustrates

how the limitation works.

Table 2
ILLUSTRATION OF DISALLOWANCE OF ITEMIZED DEDUCTIONS

	Taxpayer without Mortgage	Taxpayer with Mortgage
Income	$200,000	$200,000
Personal Exemptions family of 4a/	-$8,200	-$8,200
Itemized Deductions	-$30,000	-$40,000
It is assumed that the itemized deductions for the taxpayer with the mortgage are $10,000 higher than the itemized deductions of the taxpayer without the mortgage.		
"Disallowed" amount 200,000 - 100,000 x 0.03 =	$3,000	$3,000
The disallowed amounts are the same because the amount does not depend on the type or amount of itemized deductions.		
Taxable Income	$164,800	$154,800
Taxable income is $10,000 lower for the taxpayer with the mortgage. While the taxable incomes for both taxpayers would be lower in the absence of the "disallowance" -- $161,800 for the taxpayer without a mortgage -- $151,800 for the taxpayer with a mortgage, the $10,000 difference between the taxable incomes of the two taxpayers remains the same.		

a/ This example disregards the new phase-out of the tax benefit from personal exemptions. This is not relevant for this example.

Source: House Budget Committee, Leon E. Panetta, Chairman, "Fiscal Year 1991 Budget Agreement, Summary Materials," October 27, 1990, p.30.

HOW WILL HOUSEHOLDS FARE?

Households on all rungs of the economic ladder will be affected by the new budget and housing legislation.

Low- and moderate-income households are the target of the myriad HOPE programs. They also will benefit from new investment in affordable housing encouraged by the Low-Income Housing Tax Credit. Finally, the Low-Income Housing Preservation and Resident Homeownership Act of 1990 provides owners of federally-assisted housing with fair market incentives to maintain their buildings as low-income housing, thereby minimizing displacement of tenants as contracts expire.

Middle-income households will be hurt by some elements of the bill and helped by others. The permanent increase in the FHA loan limit will enable first-time home buyers in high-cost areas to use FHA mortgages. At the same time, risk-based premiums on FHA loans and the restrictions on the FHA loan amount could increase both the upfront and annual costs of homeownership. Some prospective first-time home buyers will be assisted by the National Homeownership Trust, which will provide down payment assistance and below-market interest rate mortgages for eligible households. The continuation of the mortgage revenue bond program will further increase the availability of below-market interest rate mortgages.

High-income homeowners will be affected by the limitation on the income tax deductions they are allowed to take. It is important to remember however that the limitations are based on their incomes, not the amount of their deductions. So the amount of disallowed deductions will be the same for taxpayers with the same incomes, regardless of whether or not they have mortgage debt on their residences.

by
Mary B. Schwartz
Housing Economist
Housing Research

Lorraine Voss
Research Assistant
Housing Research

[1] There are a few other conditions under which

the extended use period may be terminated. For a detailed account, see article in November 12, 1990 Housing and Development Reporter, "Low-Income Housing Tax Credit Extended, Revised by Budget Bill."

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U.S. Economic Outlook: December 1990

Quarterly figures are seasonally adjusted annual rates

	90.2	90.3	90.4	91.1	91.2	91.3	91.4	92.1	1988	1989	1990	1991	1992
U.S. Economy													
Annual Growth Rate													
Real GNP	0.4	1.7	-1.4	-1.5	-0.5	2.5	3.3	3.2	4.5	2.5	1.0	0.1	2.8
Industrial Production	4.3	3.7	-3.7	-0.8	-1.4	2.6	3.7	3.3	5.4	2.6	1.2	0.1	3.1
Civilian Employment	0.7	-1.5	-1.1	-0.6	-0.7	0.1	0.9	1.3	2.3	2.0	0.5	-0.6	1.1
GNP Inflation Index	4.7	4.0	4.5	5.5	3.2	2.3	2.7	3.1	3.3	4.1	4.2	4.1	2.7
Consumer Prices	3.7	6.4	7.9	7.0	2.6	1.8	2.7	3.1	4.1	4.8	5.5	5.1	2.9
Value of the U.S. Dollar	-2.0	-20.7	-21.7	-5.6	1.0	5.2	1.0	-1.2	-4.3	6.2	-9.8	-8.0	0.4
Percent													
Mfg. Capacity Utilization	82.8	82.7	81.5	81.3	80.7	80.9	81.4	81.7	83.9	83.9	82.4	81.1	82.4
Civilian Unemployment	5.3	5.6	5.9	6.2	6.5	6.7	6.7	6.6	5.5	5.3	5.5	6.5	6.4
Percent of GNP													
Federal Tax Receipts	20.3	20.4	20.5	20.6	20.4	20.4	20.5	20.7	20.0	20.2	20.3	20.5	20.7
Federal Expenditures	23.4	23.0	23.3	23.5	23.5	23.5	23.3	23.4	22.9	22.8	23.2	23.4	23.1
Federal Budget Deficit	-3.0	-2.6	-2.7	-2.9	-3.1	-3.0	-2.8	-2.6	-2.9	-2.6	-2.9	-2.9	-2.4
Interest Rates, Percent													
Federal Funds Rate	8.2	8.2	7.7	7.4	7.1	7.1	7.3	7.5	7.6	9.2	8.1	7.2	7.6
3-Month T-Bill Rate	7.7	7.5	7.0	6.7	6.5	6.5	6.7	6.8	6.7	8.1	7.5	6.6	6.9
Prime Rate	10.0	10.0	9.9	9.8	9.5	9.4	9.6	9.7	9.3	10.9	10.0	9.6	9.7
Discount Rate	7.0	7.0	7.0	6.7	6.4	6.2	6.3	6.4	6.2	6.9	7.0	6.4	6.5
Corporate AAA Bond Yield	9.4	9.4	9.3	9.0	8.9	8.8	8.9	8.9	9.7	9.3	9.3	8.9	8.9
30-Year Government Bond Yield	8.7	8.8	8.6	8.3	8.2	8.1	8.2	8.2	9.0	8.4	8.6	8.2	8.2
Mortgage Rates, Percent													
30-Year Fixed Rate	10.3	10.1	10.0	9.7	9.5	9.5	9.6	9.6	10.3	10.3	10.1	9.6	9.6
1-Year Adjustable	8.6	8.4	8.2	8.1	8.0	8.0	8.0	8.1	8.5	9.3	8.3	8.0	8.1
Home Sales & Starts													
Thousands													
Total Single-Family Sales (Single-family resales plus 97% of single-family starts)	4,188	4,166	3,905	3,917	3,955	4,060	4,181	4,266	4,648	4,446	4,183	4,028	4,326
Existing Single-Family Sales	3,320	3,333	3,090	3,117	3,139	3,211	3,302	3,366	3,594	3,467	3,292	3,192	3,422
New Single-Family Sales	540	527	487	476	466	470	488	501	676	654	536	475	512
Housing Starts	1,204	1,130	1,043	1,030	1,065	1,116	1,165	1,201	1,491	1,386	1,208	1,094	1,220
Single-Family Units	895	858	840	825	842	875	906	927	1,086	1,010	919	862	932
Multi-Family Units	309	272	203	205	223	241	259	274	405	377	289	232	288
2-4 Family Units	44	31	23	23	25	27	29	31	59	55	35	26	33
5+ Family Units	265	241	180	181	198	214	229	242	347	321	254	206	255
Mobile Homes Shipped	190	187	191	187	187	193	200	202	218	199	191	192	203
Percent change – Year Ago													
Total Single-Family Sales	-2.7	-5.5	-13.1	-12.4	-5.6	-2.5	7.1	8.9	0.4	-4.3	-5.9	-3.7	7.4
Existing Single-Family Sales	-0.6	-3.2	-12.6	-8.9	-5.5	-3.7	6.9	8.0	2.4	-3.6	-5.1	-3.0	7.2
New Single-Family Sales	-15.1	-24.7	-25.3	-19.7	-13.7	-10.7	0.2	5.4	0.8	-3.3	-17.9	-11.5	7.8
Housing Starts	-1.1	-15.5	-22.6	-29.2	-11.5	-1.2	11.7	16.6	-8.6	-7.0	-12.9	-9.4	11.5
Single-Family Units	-1.0	-13.8	-15.0	-23.8	-5.9	2.0	7.9	12.4	-5.9	-7.0	-9.0	-6.2	8.1
Multi-Family Units	-1.5	-20.4	-43.6	-44.9	-27.7	-11.4	27.7	33.7	-14.9	-7.1	-23.3	-19.7	23.9
2-4 Family Units	-1.8	-44.6	-56.7	-46.2	-41.7	-11.4	27.7	33.7	-10.0	-5.7	-36.4	-25.1	23.9
5+ Family Units	-1.4	-15.7	-41.3	-44.7	-25.4	-11.4	27.7	33.7	-15.7	-7.3	-21.0	-18.9	23.9
Median Home Prices													
Thousands of Dollars													
Existing Home Prices	96.2	96.6	92.8	93.1	95.2	96.1	97.8	99.0	89.2	92.9	95.4	95.6	100.7
New Home Prices	126.7	116.7	117.8	118.1	119.2	120.2	121.7	124.3	113.4	120.4	121.1	119.8	126.5
Percent Change - Year Ago													
Existing Home Prices	3.5	1.7	0.1	-3.0	-1.0	-0.5	5.4	6.3	5.0	4.2	2.6	0.2	5.3
New Home Prices	6.0	-2.5	-5.3	-4.1	-5.9	3.0	3.3	5.2	8.3	6.2	0.6	-1.1	5.6

Source: Forecast produced using Laurence H. Meyer & Associates' model of the U.S. economy.
Assumptions and simulations by Dr. John Tuccillo, Robert Barr and Kim Martin.

The *Real Estate Outlook* features a monthly summary of current economic conditions, an easy-to-read forecast for the economy and real estate, and selected reports on issues affecting the housing industry. In addition, one of the Nation's top real estate economists, Dr. John Tuccillo, gives his commentary on the state of the economy and its implications for real estate markets. If you would like to subscribe to the *Real Estate Outlook*, contact the Forecasting and Policy Analysis Division at (202) 383-1131. The annual subscription fee is $25 for members of the NATIONAL ASSOCIATION OF REALTORS® and $30 for nonmembers.

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Vol. 4, No. 1

OUTLOOK

January 1991

A Monthly Forecast for the Economy and Real Estate

FORECAST SUMMARY

- The nation's economy has slipped into a recession, as industrial production figures and employment data show that the economy is in retreat on many fronts. Yet several factors suggest that this recession will be milder than the typical downturn. Inventories are in better shape; exports appear healthy; interest rates have already fallen significantly; and the credit crunch appears limited to commercial real estate projects, not to the economy as a whole.
- The two halves of 1991 are expected to be quite different. During the first half, the economy is projected to contract at a 1.2 percent annual rate. But lower interest rates, stronger export activity and renewed consumer confidence should allow for 3.0 percent annual growth in the second half of the year.
- A robust 9.3 percent increase in the pace of housing starts during November broke a nine-month string of declines. Rather than a sign of a reviving economy, the figure probably represents a rebound from October's large 6.6 percent decline to a more sustainable level of starts activity. Housing starts are not expected to reach bottom until the first quarter of 1991. A recovering economy and lower mortgage rates will spur home building in the second half of 1991.
- The new home sales rate climbed back over the half-million mark in November, and sales are expected to average 495,000 in the final quarter of 1990, down 6.1 percent from the third quarter. With housing starts expected to continue its descent during the projected mild recession, sales of new homes will also be falling. On a brighter note, mortgage rates have already started falling, and, by the second half of 1991, the economic recovery will foster an increase in demand for new homes.
- Existing home sales posted a 3.0 percent gain in November. The increase follows two months of significant declines. Despite the rebound, the market remains troubled. Sales for 1990 are expected to be 5 percent below 1989's sales volume. The worst may be behind us, however, as lower mortgage rates will lead to modest gains in the first half of 1991, and economic recovery in mid-1991 should further spur the market.

IN THIS ISSUE

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You Fret Your Life

by John A. Tuccillo
Chief Economist and Senior Vice President
Real Estate Finance

Anyone with children knows that you spend your life worrying about the wrong things. Most of the time it's like that with the economy as well -- maybe that's just the fate of mankind. So, as we begin the new year, we offer some things that should be worrisome.

But first, let's examine what the body politic is concerned with. Such a list would include (in no particular order) the prospects for war in the Gulf; the deterioration of society caused by drugs, a failing educational system and a growing underclass; the precarious state of the financial system; slumping housing markets; the Federal deficit; impending recession; and competition from abroad.

All of these are important, of course, since any one or all of them will impact our individual and collective lives in the short term. But we can do little about them now. In every case, there are forces in motion -- the will of Saddam Hussein, the state of Japanese technology and organization, the Congressional budget process (among others) -- that will determine their impact on our society. Worry is a natural, but impotent, response.

Yet each one of these cares comes from the seed of a longer term concern about which we can do something, and therefore should worry. The early years of the Nineties will be a period of almost continual change in all areas, including the economy. By worrying now for the future, we can make those changes we must to shape that future. Let's look at each of these:

1. The banks are going to fail. No, they're not. Despite the rush to hitch the commercial banking system to the savings and loan millstone, the differences are legion. Right now, the problem loans at banks are increasing and putting a strain on the insurance fund, but not enough to sink it. But in the future the evolution of financial services that has so transformed the familiar landscape of the banking system will only accelerate as new, uninsured, transnational channels for the flow of funds come into prominence. Nowhere will this be felt more than in real estate finance (in its broadest form). If we can shape this change the right way, the flow of funds to real estate in the future will be secure. Let's worry about that.

2. Housing markets are in deep trouble. Not in the long run, although an index based on the price of reporters' homes in Northern New Jersey may lead you to think so. The nature of housing is to be cyclical, as soaring prices bring oversupply and then correction. The longer the market soars, the longer the correction will be. It has been ever thus, and so it will be. That doesn't take the sting out of the Northeast but does explain what's happened (and is happening) in Houston and Dallas. But, the population is changing and before the end of the decade those changes will crucially affect the real estate business. The aging postwar generation will see its own American dream change from the suburban center hall colonial with a quarter acre to a low maintenance, high amenity condo in reach of leisure activities. Realtors don't build houses, but we do deal with people and adapting to these changes will be a real challenge. That's worth worrying about.

3. Tinhorns like Saddam will be a continual thorn in the side of the U.S. Maybe, and maybe not: it all depends on how we will deal with the tinhorn *de jour*. War in the current instance seems like a tragic overreaction but may serve to extinguish like ideas in others. Yet, it's probably more important what we do afterwards. The Nineties will see increasing economic pressure from the growing populations of not only the Muslim world, but also Latin America, Africa and South Asia. In addition, those new citizens of the Third World in Eastern Europe and the Soviet Union will seek the means of development. There's only one source to meet these demands -- the industrialized nations. A failure to integrate successfully the have-nots into the community of developed nations will be the surest cause of continual conflict. This is a global worry.

4. We're saddled forever with a profligate public sector. Growing savings from the postwar generation and an exploding Social Security Trust Fund ought to make current deficits a memory by the mid-Nineties. But by that time, the U.S. must have made a decision to invest more into its capital resources. The private sector needs to modernize its plant to compete in a world market; the public sector needs to replace the bridges, tunnels, and roads that link us. Most importantly, we need to make a major investment in human capital to build our educational systems and to reclaim those resources being destroyed in our cities. That may be the biggest worry of all.

No economy exists by itself. It is fed and nourished by a financial system and shaped and controlled by a political system. What really makes this a time of anxiety is that the three are out of synch. With its capacity to move any amount of funds across any distance instantaneously at anytime, the financial sector is leading us into the Twenty-first Century. Our economy, advanced in some areas and laboring in others, is still rooted in the Twentieth Century. Our political system, with its continued stress on turf and national identity, is firmly mired in the Nineteenth Century. And as the challenges build around us, the real worry is whether we can line these three up in a way that will let us solve the riddle of the future.

By now, you're reaching for the aspirin bottle, and it's not because of New Year's Eve. But, as the ghost of Christmas future told Scrooge, these are only things that *might* be, not *will* be. Or, in the words of Groucho Marx, "It's been very pleasant talking to you, but now it's time to play the game."

Outlook for the Economy and Real Estate

The sounds you've been hearing from the nation's economic data mills are the sour notes of a recession. The nation's economy is contracting -- and at a sharper pace than had been generally anticipated. The tenor of the most recent statistics is that the weakness is becoming increasingly widespread. Both the industrial production figures and the employment report show that the economy is in retreat on most fronts.

Yet several factors suggest that this recession will be milder than the typical downturn. (For more details on how this downturn stacks up with the eight previous post-World War II recessions, see pages 8-11.) Inventories are in better shape; exports appear healthy; interest rates have already fallen significantly; and the credit crunch appears limited to commercial real estate projects, not to the economy as a whole.

The projections presented here assume a diplomatic solution to the Persian Gulf crisis. The outbreak of a shooting war would deepen and lengthen the recession as oil prices rise. Interest rates would shoot up, and consumer confidence may sink further. One key to the war's impact on the economy would be any damage done to oil fields and pipelines in the Mideast.

Fourth Quarter of 1990 Turns Down

It appears that the recession began sometime between August and October, and that the fourth quarter of 1990 will be the first quarter in which the economy recorded negative growth. NAR's current forecast places this figure at an annual rate of 2.2 percent. Estimates from an informal survey of the nation's top economists on the fourth quarter's contraction range from 2.0 percent to 3.0 percent.

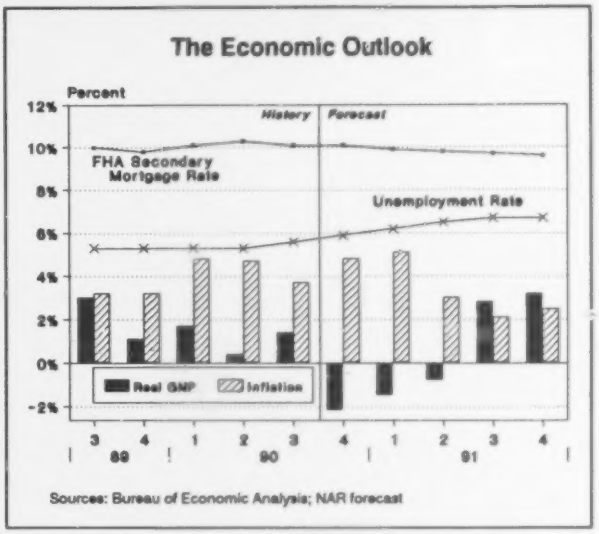
With the Federal Reserve's more aggressive easing in recent weeks, this month's forecast projects significantly lower interest rates than previously forecasted. Mortgage rates, for example, were expected to average 9.6 percent in both 1991 and 1992 in last month's outlook, but are now anticipated to average 9.2 percent in 1991 and 9.0 percent in 1992. By having the usual stimulative effect in housing and other markets, the lower interest rates will play an important role in keeping the recession mild.

Consumers Call the Tune

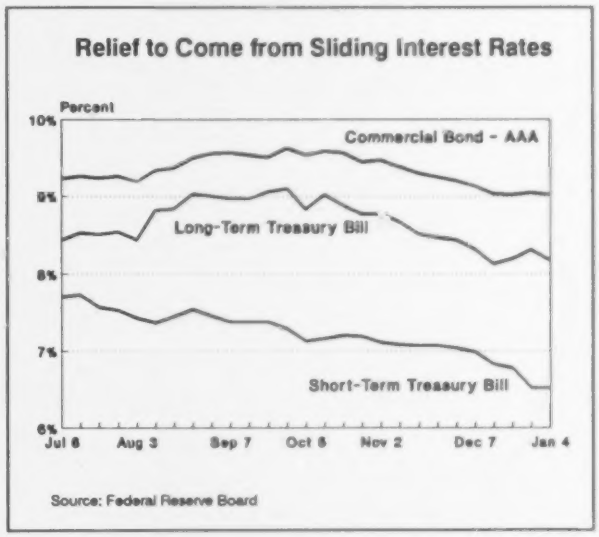
This recession appears to be different than the typical postwar recession: Worried consumers rather than battered businesses seem to be calling the tune. Generally, consumers, while trimming their spending growth, add at least some strength to the economy during a recession. Businesses, meanwhile, find themselves with bloated inventories at the outset of a recession and consequently cut production drastically. But this time businesses appear to have kept inventories in check -- while shaky consumer confidence, eroding real personal income, and high debt levels have led consumers to keep their checkbooks closed.

Employment Stronger Than Expected

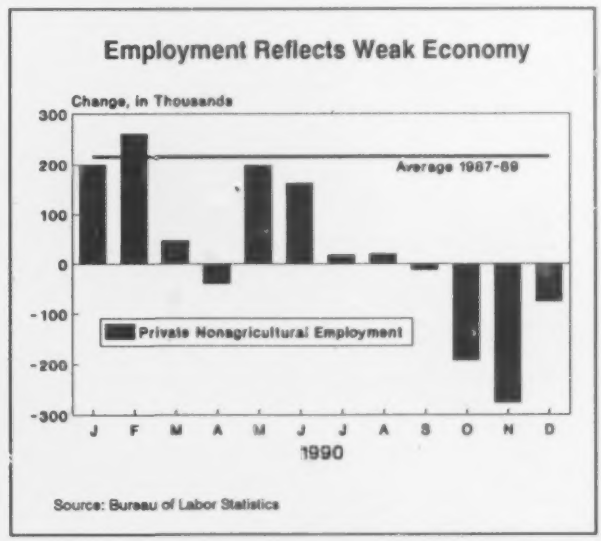
While marking the sixth consecutive monthly decline in payroll employment, December's loss of 76,000 workers was much more modest than November's decline of 259,000. Many analysts had expected a much larger decline in December, and the relatively small decline is



Sources: Bureau of Economic Analysis; NAR forecast



Source: Federal Reserve Board



Source: Bureau of Labor Statistics

another indication that the recession will be mild. The unemployment rate in December rose to 6.1 percent, its highest level in over two years.

Widespread Weakness in Industrial Production

Industrial production dropped sharply at year end, falling at a 10.4 percent annual rate between September and November. The data confirms the widely recognized difficulties in the automotive industry as the production of automotive products fell at an astounding 38.3 percent annual rate between September and November. But the most striking feature of the data is that the weakness is not isolated. Production of other consumer durable goods during this period was down by a 15.4 percent annual rate, and nondurable goods, such as food, clothing, and energy, fell 5.8 percent. Of the one dozen major market groupings for consumer goods, an increase was registered in only one category: paper products, up 4.1 percent.

The weakness was not limited to consumer goods, as production of business equipment dropped at a 7.4 percent annual rate between September and November. Defense equipment, even during the period when the U.S. was gearing up for Operation Desert Shield, experienced a 4.4 percent decline. The bottom line on the industrial production figures is that the downturn has spread from a few troubled industries to encompass much of the economy.

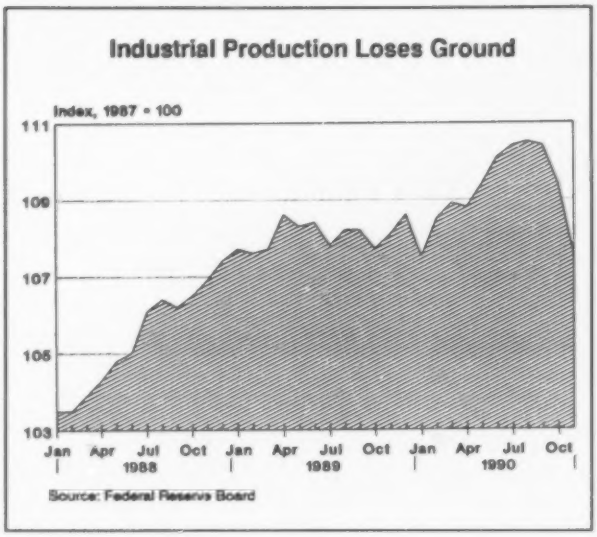
Low Money Growth Gives the Fed More Room to Ease

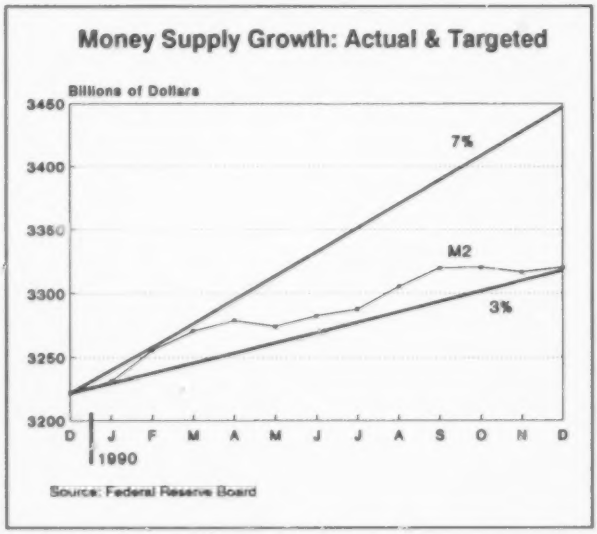
The monthly employment reports induced the Federal Reserve to ease monetary policy by lowering the target ranges on the closely-watched fed funds rate. After spending most of October and early November around 8.0 percent, the fed funds rate fell to 6.5 percent by the first week of the new year. Another key short-term interest rate, that on 3-month Treasury Bills, sunk below 6.5 percent in early January, a full point below its level in mid-August.

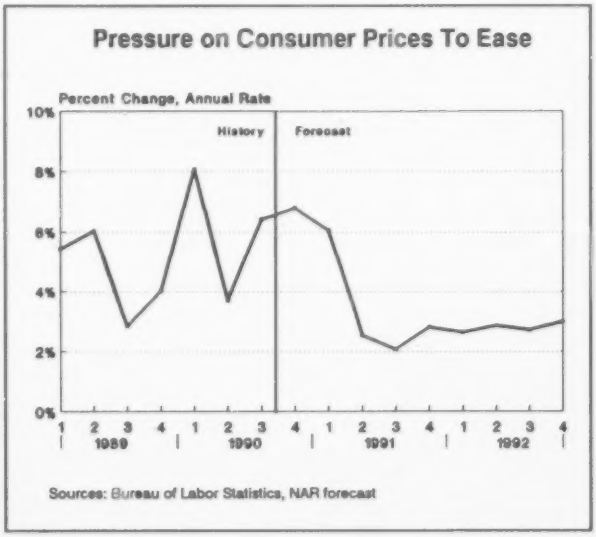
The Fed was also prompted to act by the sluggish growth seen in the money supply measure known as M2, since too little money growth is a sign of a faltering economy. For 1990, the Fed targeted M2 growth between 3 and 7 percent. By easing credit policy over the last few weeks, the Fed hopes to encourage bank lending, an activity which increases the money supply, and, presumably, economic activity. Too much money growth, of course, leads to higher inflation, but M2 is in danger of falling below the Fed's lower target range, as shown in the chart at right. During the 1982-89 expansion, M2 growth averaged 7.4 percent per year; in the 12 months since December 1989, M2 has grown at a 3.1 percent rate.

A Jeckyl and Hyde Economy in 1991

The two halves of 1991 are expected to be quite different. During the first half, the economy is projected to contract at a 1.2 percent annual rate. But lower interest rates, stronger export activitiy and renewed consumer confidence should allow for 3.0 percent annual growth in the second half of the year. This represents a recovery more modest than most, but then the recession itself is expected to be milder than usual. For the year, the economy will contract 0.2 percent, relative to 1990's sluggish 0.9 percent gain. The recovery should continue into 1992, with the economy growing 2.9 percent.







Housing Starts

(Seasonally Adjusted Annual Rates, in Thousands)

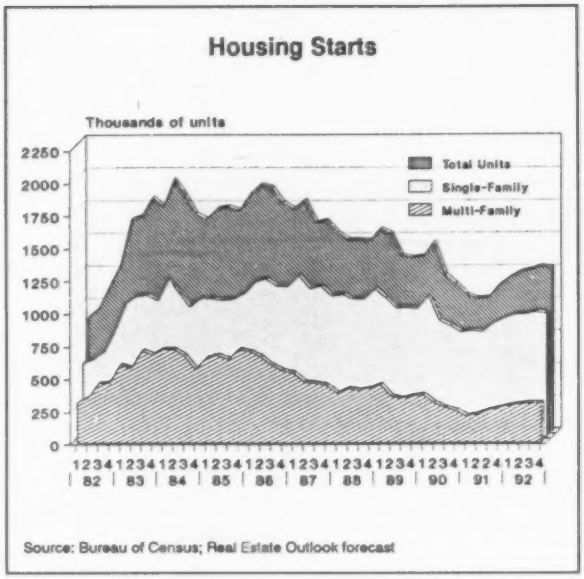
National Data

	Total	SF	2-4	5+
Nov 1989	1,347	1,010	47	290
Jul 1990	1,153	875	29	249
Aug 1990	1,131	836	30	265
Sep 1990	1,106	859	34	213
Oct 1990	1,033	856	21	156
Nov 1990	***1,129***	***772***	***43***	***314***
Annual Averages:				
1988	1,491	1,086	59	347
1989	1,386	1,010	55	321
Percent Changes in November 1990 since:				
Nov 1989	-16.2	-23.6	-8.5	8.3
Oct 1990	9.3	-9.8	104.8	101.3

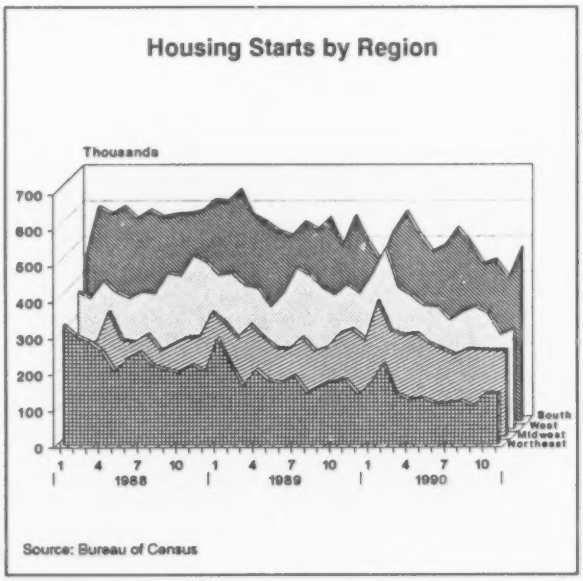
Regional Data

	Northeast	Midwest	South	West
Nov 1989	179	296	498	374
Jul 1990	113	225	493	322
Aug 1990	120	241	434	336
Sep 1990	104	239	445	318
Oct 1990	142	237	394	260
Nov 1990	***140***	***237***	***478***	***274***
Annual Averages:				
1988	240	273	574	404
1989	183	270	536	397
Percent Changes in November 1990 since:				
Nov 1989	-21.8	-19.9	-4.0	-26.7
Oct 1990	-1.4	0.0	21.3	5.4

Source: Bureau of Census, Construction Reports, Series C25



Source: Bureau of Census; Real Estate Outlook forecast



Source: Bureau of Census

A robust 9.3 percent increase in the pace of housing starts during November broke a nine-month string of declines. Rather than a sign of a reviving economy, the figure probably represents a rebound from October's large 6.6 percent decline to a more sustainable level of starts activity. The annual rate of 1,129,000 units is 16.2 percent below the rate recorded in November 1989, and the levels reached during the fourth quarter of 1990 are the lowest since the end of the last recession in October 1982. Relative to the first eleven months of 1989, the pace of housing starts so far this year is down 11 percent. Single-family starts are down 8 percent; multi-family starts are down over 19 percent.

All of November's gain is accounted for by multi-family housing starts. The rate of starts doubled from 177,000 units in October to 357,000 units in November. Again, the jump in November probably does not signal renewed strength in the housing markets; rather, it likely represents a return from a very poor October. As a comparison, multi-family starts averaged 318,000 units nine months of 1990.

Almost 90 percent of November's increase occured in the South, where starts were up 21.3 percent.

Housing starts are not expected to reach bottom until the first quarter of 1991, when they are projected to average 1,022,000 units. A recovering economy and lower mortgage rates will spur home building in the second half of 1991, and healthy gains in 1992 are expected as well.

New Home Sales

(Seasonally Adjusted Annual Rates, in Thousands)

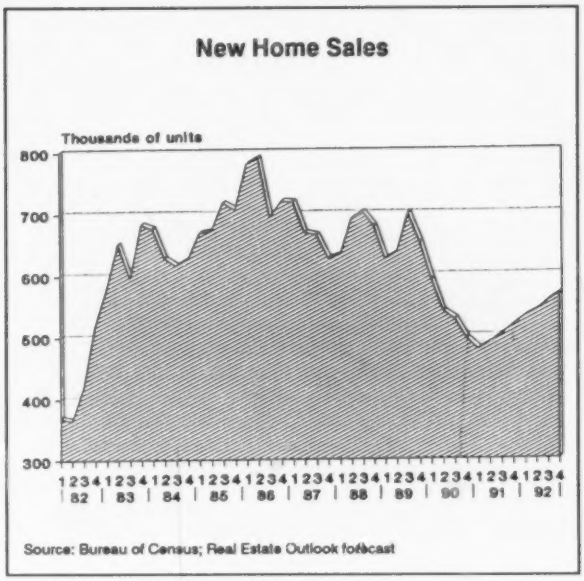
National Data

		Mo. Ago % Chg.	Yr. Ago % Chg.
Nov 1989	687	8.0	5.7
Dec 1989	633	-7.9	-5.4
Jan 1990	613	-3.2	-12.9
Feb 1990	606	-1.1	-2.7
Mar 1990	558	-7.9	0.4
Apr 1990	533	-4.5	-12.6
May 1990	536	0.6	-17.7
Jun 1990	550	2.6	-14.9
Jul 1990	541	-1.6	-27.0
Aug 1990	527	-2.6	-26.7
Sep 1990	507	-3.8	-20.5
Oct 1990	492	-3.0	-22.6
Nov 1990	***506***	***2.8***	***-26.3***
Annual Averages:			
1988	676		0.8
1989	654		-3.3

Regional Data

	Northeast	Midwest	South	West
Nov 1989	96	117	263	211
May 1990	71	91	215	159
Jun 1990	80	94	233	143
Jul 1990	70	93	238	140
Aug 1990	63	88	238	138
Sep 1990	56	96	219	136
Oct 1990	80	78	223	112
Nov 1990	***81***	***84***	***221***	***120***
Annual Averages:				
1988	101	98	271	206
1989	90	103	258	202
Percent Changes in November 1990 since:				
Nov 1989	-15.6	-28.2	-16.0	-43.1
Oct 1990	1.3	7.7	-0.9	7.1

Source: Bureau of Census, Construction Reports, Series C25



The new homes sales rate climbed back over the half-million mark in November, when the annual pace rose 14,000 units to 506,000 units. While the increase is welcome news, it stands as only one of three months in the previous twelve that sales increased, and the month's sales pace was more than one-quarter below the sales rate of November 1989.

The Northeast was able to extend its impressive October increase into November, generating a sales pace in these two months that was almost 8 percent higher than the average sales rate of the year's first nine months. While remaining almost 16 percent below the rate set in November 1990, the month was the strongest in the region since April. The Midwest and the West registered strong gains in November, up 7.7 percent and 7.1 percent, respectively. The South dropped almost one percent.

Sales of new homes are expected to average 495,000 in the final quarter of 1990, down 6.1 percent from the third quarter. With housing starts expected to continue its descent during the projected mild recession, sales of new homes will also be falling. The bottom will be reached in the first quarter of 1991, when the sales rate is expected to reach 478,000 units. Mortgage rates have already started falling, and, by the second half of 1991, the economic recovery will foster an increase in demand for new homes. The buying opportunities afforded by lower mortgage rates and rising incomes in late 1991 and into 1992 may catch home builders short of supply.

Existing Single-Family Home Sales

(Seasonally Adjusted Annual Rates, in Thousands)

National Data

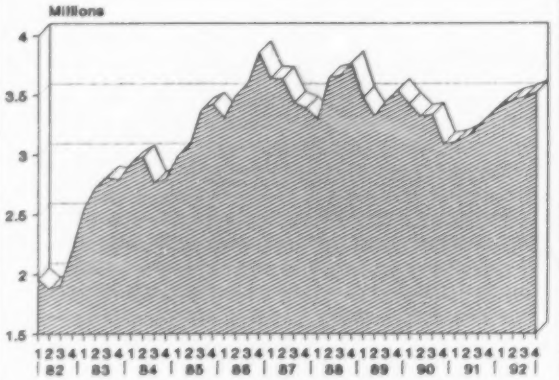
		Mo. Ago % Chg.	Yr. Ago % Chg.
Nov 1989	3,560	2.0	-4.0
Dec 1989	3,560	0.0	-9.2
Jan 1990	3,470	-2.5	-5.2
Feb 1990	3,400	-2.0	-4.2
Mar 1990	3,400	0.0	-0.9
Apr 1990	3,330	-2.1	-3.2
May 1990	3,300	-0.9	1.5
Jun 1990	3,330	0.9	0.0
Jul 1990	3,330	0.0	-1.5
Aug 1990	3,500	5.1	1.7
Sep 1990	3,170	-9.4	-9.7
Oct 1990	3,050	-3.8	-12.6
Nov 1990	***3,140***	***3.0***	***-11.8***
Annual Averages:			
1988	3,594		-1.9
1989	3,467		-3.6

Regional Data

	Northeast	Midwest	South	West
Nov 1989	590	950	1,390	630
Jun 1990	490	960	1,310	580
Jul 1990	560	930	1,310	530
Aug 1990	520	990	1,400	570
Sep 1990	520	870	1,260	520
Oct 1990	500	820	1,230	490
Nov 1990	***490***	***820***	***1,320***	***500***
Annual Averages:				
1988	669	929	1,348	643
1989	590	931	1,320	617
Percent changes in November 1990 since:				
Nov 1989	-16.9	-13.7	-5.0	-20.6
Oct 1990	-2.0	0.0	7.3	2.0

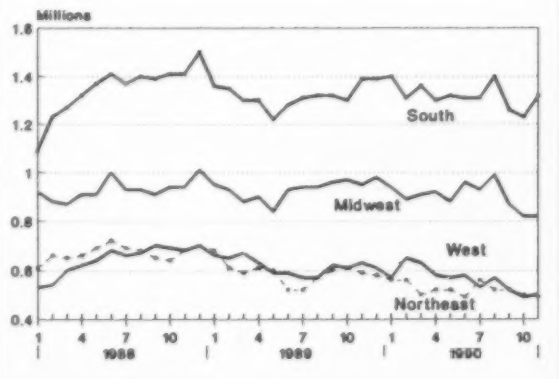
Source: National Association of Realtors,® "Home Sales"

Existing Home Sales



Source: NAR Economics & Research; Real Estate Outlook forecast

Existing Home Sales by Region



Source: NAR Economics & Research

Existing home sales posted a 3.0 percent gain in November, with the sales rate at 3,140,000 units. The increase follows two months of significant declines and comes despite declining activity in many key areas of the economy. As was true for housing starts, the strength came from the South, which was up 7.3 percent. A small gain in the West was countered by a small drop in the Northeast, and the Midwest held steady in November.

Despite the rebound, the market remains troubled. Sales in the three-month period ending in November were down 7.9 percent over sales in the previous three month period, and sales for 1990 are expected to be 5 percent below 1989's sales volume. After a 2.7 percent decline in 1991, sales are expected to rebound by 8.2 percent in 1992.

In terms of sales declines, however, the worst may be behind us. Although sales for the year are expected to be down in 1991, the fourth quarter of 1990 is expected to turn out to be the low point for sales. Lower mortgage rates will lead to modest gains in the first half of 1991, and economic recovery in mid-1991 should boost job growth and incomes to further spur the market. Relative to the fourth quarter 1990 figure, the annual rate of increase in sales is expected to be 3.9 percent during the first half of 1991 and 11.7 percent during the second half. Like the other forecasts in this publication, this projection depends importantly on the peaceful resolution of the Gulf crisis.

Single-Family Home Prices

(In Dollars)

National Data

	Median		Average	
	Existing	New	Existing	New
Nov 1989	93,100	125,000	117,900	151,400
Jun 1990	97,500	125,000	121,100	150,400
Jul 1990	98,300	118,700	122,000	149,800
Aug 1990	97,100	118,400	120,500	144,700
Sep 1990	94,400	112,200	116,700	142,100
Oct 1990	92,900	120,000	115,900	153,200
Nov 1990	***91,300***	***121,500***	***115,200***	***146,500***
Annual Averages:				
1988	89,200	113,400	112,500	138,900
1989	92,900	120,400	118,000	148,300
Percent changes in November 1990 since:				
Nov 1989	-1.9	-2.8	-2.3	-3.2
Oct 1990	-1.7	1.3	-0.6	-4.4

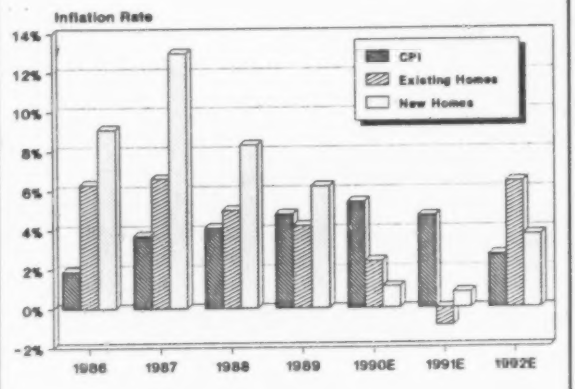
Regional Data

Median Prices for Existing Single-Family Homes

	Northeast	Midwest	South	West
Nov 1989	145,700	71,400	82,200	147,100
Jun 1990	148,300	75,900	87,500	138,100
Jul 1990	146,900	76,000	88,800	139,700
Aug 1990	145,300	75,300	86,900	140,200
Sep 1990	137,100	74,200	85,900	134,700
Oct 1990	136,200	72,000	83,200	142,000
Nov 1990	***133,600***	***71,700***	***83,200***	***138,700***
Annual Averages:				
1988	142,500	68,200	82,200	124,700
1989	145,100	71,200	84,400	139,800
Percent changes in November 1990 since:				
Nov 1989	-8.3	0.4	1.2	-5.7
Oct 1990	-1.9	-0.4	0.0	-2.3

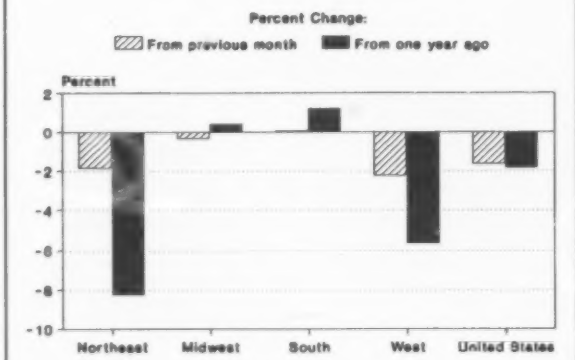
Source: National Association of Realtors,® "Home Sales"

Home Prices



Source: Bureau of Census; E Real Estate Outlook forecast

Home Prices by Region



Source: NAR Economics & Research

The median price of existing homes fell by 1.7 percent in November to $91,300, $1,600 below October's level. The median price has fallen for four consecutive months and now stands $7,000 below its recent peak in July. The figure is about 2 percent below its year-ago level. The median price for new homes, on the other hand, built on last month's 7.0 percent increase, adding another 1.3 percent to stand at $121,500 in November. This rebound comes after the median price for new homes had dropped $12,800, or 10.2 percent, between June and September. Relative to its level of a year ago, the median price is down by almost 3.0 percent.

Average prices for both existing and new homes fell in November. For existing homes, the average price fell by 0.6 percent to $115,200. The drop was more dramatic for new homes, where average prices slipped 4.4 percent.

The median price of existing homes is projected to drop almost 1 percent in 1991, relative to 1990. Prices are expected to firm as the recovery takes hold and buyers take advantage of lower mortgage rates. An increase of 6.4 percent is projected for 1992.

Robert D. Barr
Director of Forecasting
Forecasting & Policy Analysis Division

How Will This Recession Stack Up?

Tiring consumers and the Federal Reserve's inflation-fighting monetary policy brought slow growth to the U.S. economy over the last couple of years. In the last few months, with uncertainty over war and a shock in oil prices, both employment and industrial production have made U-turns. It's apparent that a recession has settled in. Despite this gloomy assessment, the current NAR forecast is relatively optimistic. The economy will not enter a free-fall; in fact, the recession is likely to be mild. Economic expansion should be well under way during the second half of 1991. In comparing the projected downturn with the track record of previous recessions, this article will present the case for a mild recession. Of course, there are sizeable risks to the economy -- particularly the threat of war in the Persian Gulf -- and these will be discussed as well.

The Eight Post-War Recessions

Peak	Trough	Duration	Depth
Nov '48	Oct '49	11	2.0%
Jul '53	May '54	10	3.0%
Aug '57	Apr '58	8	3.5%
Apr '60	Feb '61	10	1.0%
Dec '69	Nov '70	11	1.1%
Nov '73	Mar '75	16	4.3%
Feb '80	Jul '80	6	2.3%
Aug '81	Nov '82	16	3.4%
Average		11	2.6%
Current Forecast		*9*	*1.1%*

Note: Duration in months

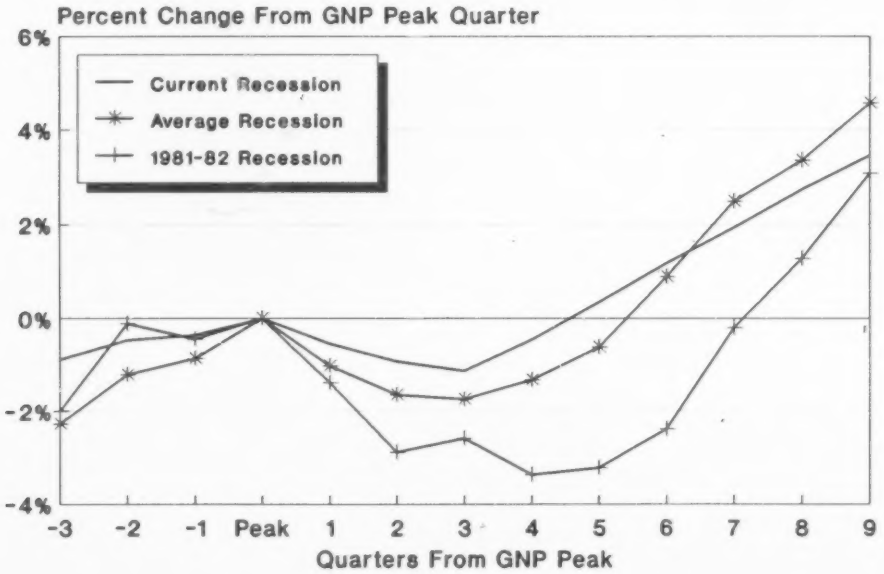
Eight Postwar Recessions

A recession is a period of sustained contraction in real GNP, or the inflation-adjusted value of output produced in the economy. The rule of thumb is that two quarters of contraction constitute a recession, but the final call is made by a panel of private-sector economists who look beyond the GNP figures to determine the economy's turning points.

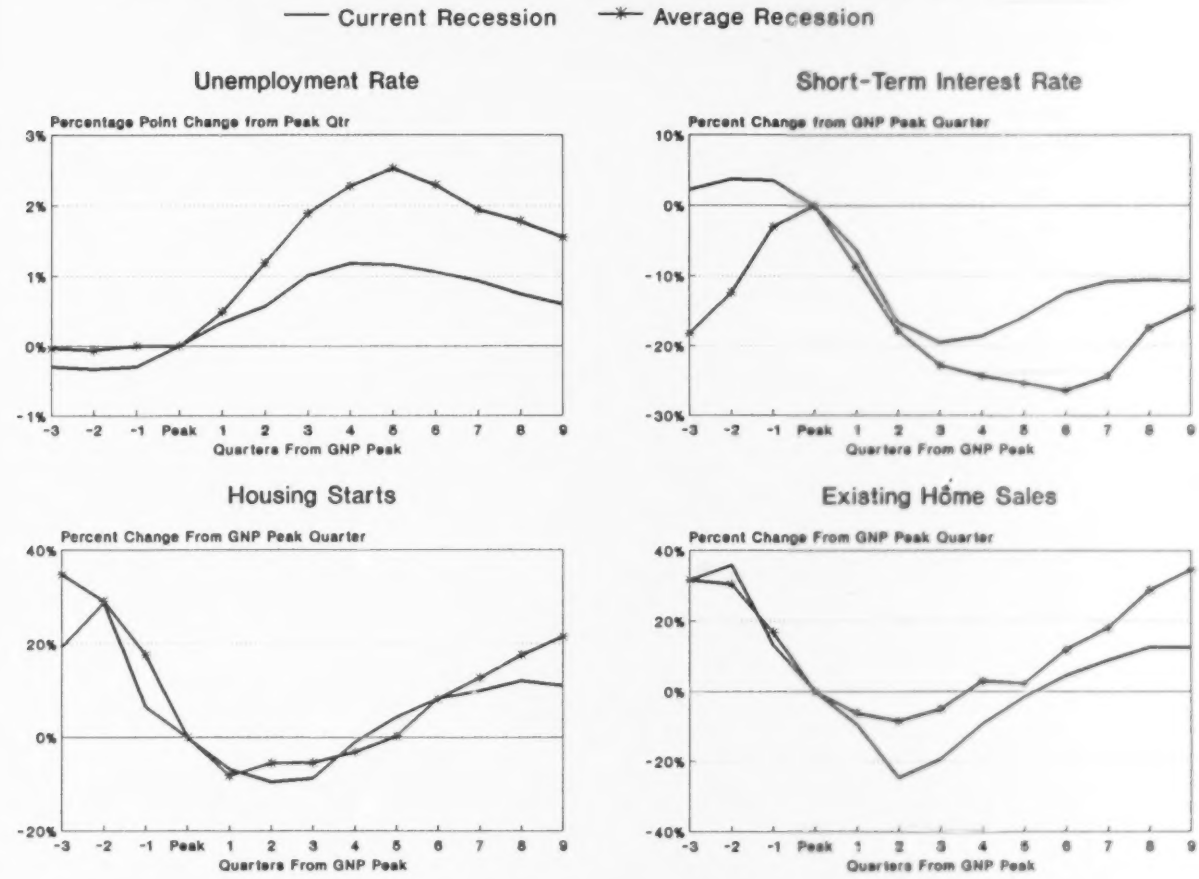
Since World War II, the U.S. economy has weathered eight recessions. The table at right shows the starting and ending dates of the recessions, that is, when real GNP started to fall and, later, when real GNP hit its low point and began to recover. Also shown for each recession are duration and depth, which measures how much the economy contracted from the peak of GNP to its trough. On average, recessions have lasted just under a year and have cut output in the economy by 2.6 percent. The table also shows that the current recession is projected to be two months shorter than the average recession, but, more importantly, that output will drop by only 1.1 percent.

This means the recession will be shallower than the average recession. The graph below shows how moderate the current recession is expected to be relative to the average downturn and the 1981-82 slump. The set of charts to the right compare the current recession to the average

Recession/Recovery Comparison: Real GNP



Recession/Recovery Comparison: Current vs. Average



recession for four additional variables, and the charts on the following page compare the current recession to the 1981-82 downturn for those same four variables.

It is interesting to note that for both housing variables, most of the decline in activity occurs in the year prior to the onset of the recession.

Why a Mild Recession?

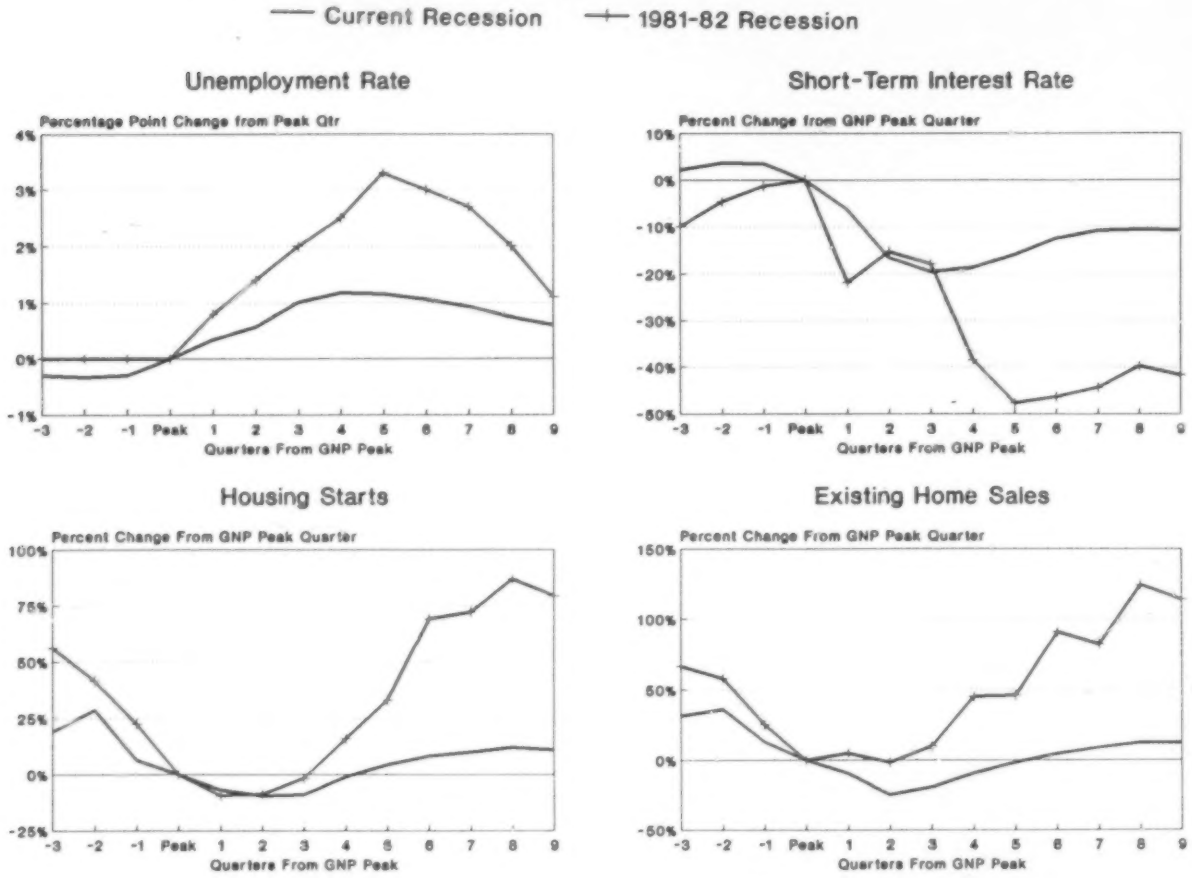
The evidence suggests that several factors are at work to moderate this recession and prepare the economy for several years of growth in the 1990s.

Interest Rates. Despite the spike in rates that occured immediately after Iraq invaded Kuwait, interest rates have been heading downward. The Federal Reserve has eased credit policy to moderate the recession, and rates have responded by falling. The rate on the 3-month Treasury Bill, the short- term interest rate used in the chart above, has fallen a full percentage point in the past six months, to an average of 6.5 percent in the first week of January. The 30-year Treasury yield has fallen a third of a percentage point to 8.2 percent in the same period. Rates on 30-year fixed mortgages have fallen almost one-half of a point. Lower rates are a key to reviving consumer and business activity.

The graph showing the change in short-term rates under the typical recession and in the current recession offers an important reason why this recession is expected to be relatively mild. First, notice how interest rates tumble during a recession. These lower rates are one element that prepares the stage for the ensuing recovery. Next, note how short term rates have typically risen almost 20 percent in the year preceding a recession. Yet this time we see that short-term rates have actually fallen in the year before GNP peaked and the recession began. In other words, interest rates were already headed in the right direction -- down -- when the recession commenced.

Inventories. Typically, the end of a expansion sees a build-up of inventories. Consumers generally begin to pull back on their purchases. Inventories rise, and businesses subsequently cut production back, selling goods out of inventories. Currently, most firms appear to have a good handle on inventories. In the two quarters immediately prior to the 1981-82 recession, inventory investment rose by almost $50 billion. In contrast, in the two quarters prior

Recession/Recovery Comparison: Current vs. 1981-82



to this recession, inventories rose only $14 billion, after adjusting for inflation. Additionally, the inventories-to-sales ratio has remained low, particularly for manufacturers.

Exports. Nonfarm exports grew a robust 8.4 percent over 1990, one of the few bright spots in the 1990 economy. Further gains are expected due to a nearly 15 percent drop in the value of the dollar over the past year. This will make U.S. goods even more attractive in foreign markets. Since most of the drop came in the last six months, the extra kick to exports from the lower dollar has yet to be felt. Of course, the falling dollar also suggests higher prices for foreign goods in the U.S. And exports may be crimped by recessions in Canada, Britian and Australia, as well as slower growth in Japan and Germany. Nevertheless, exports are in better shape now than they have been in most previous recessions.

Inflation. While inflation is not tame, it is currently under much better control today than it was on the verge of the 1981-82 recession. The more inflation initially, the longer is the costly process of unraveling inflationary pressure in the economy. Much of the decline in interest rates during the 1981-82 downturn, as depicted in the graph above, was due to falling inflation rates.

Lower Energy Costs. So far, the run-up in gasoline prices has been much less severe than the increases seen in the two oil shocks of the 1970s. Additionally, the nation is significantly more fuel efficient. In 1988, for example, the U.S. required 20 percent less oil to produce $1,000 worth of output than it did in 1979. Consequently, the squeeze on oil prices will hurt less during this recession.

Of course, this conclusion relies on a major assumption: Current projections assume either a diplomatic solution to the Persian Gulf crisis, or, at worst, a limited confrontation with little damage done to the Mideast's oil fields. If this is the case, the economy can look forward to a decline in gasoline prices. This would not only leave more money in consumers' pockets, but it would allow that money to go further by dampening the inflation rate.

Rebounding Consumer Confidence. During the fall, consumer confidence took a big plunge -- in fact, the biggest plunge of the twenty years on record according to one measure. A quick resolution to the Persian Gulf situation and the tonic of lower interest rates may lead to

sizeable gains in confidence by mid-year. This should lead to a revival of consumer activity, although the return will be less triumphant than in previous recoveries as the debt-overhang from the late 1980s will continue to plague the consumer.

Risks To the Forecast

The economy is vulnerable to several risks that could trigger a longer and deeper recession.

War in the Persian Gulf. Oil prices are expected to shoot up if war breaks out. How far depends on expectations about the length of the war, its outcome, and the damage done to oil fields, pipelines, and other facilities. Increased uncertainty will drive up interest rates, as will heightened inflation expectations due to higher oil prices. The recession will certainly run longer and deeper, though how much depends upon a host of noneconomic factors.

Financial Instability. The S&L crisis, the wobbly condition of many banks, and the increase in debt leverage leave many businesses and financial institutions vulnerable to the reduction in cash flow that generally accompanies a recession. The ratios of debt service and interest payments relative to revenues have increased, leaving the firms more financially unstable. An upward jolt in interest rates, due to war, for example, may topple many firms. In such a climate, surviving businesses may be much more reluctant to add the additional debt necessary to expand operations.

Government Policy. Two government policies in particular may harm the chances of recovery. First, the increased scrutiny of financial institutions may be having a chilling effect on lending. The credit crunch, which appears to be a factor only in the commercial real estate industry, remains a concern for residential real estate and consumer and business loans. If banks become overly cautious due to regulatory concerns, the lower interest rates will have less of an impact on reviving a recessionary economy. Second, the federal government, as well as several state governments, are raising taxes during a recession. Although raising taxes is hardly unusual, the timing is. This places another squeeze on disposable income.

How This Recession is Different

By way of concluding, we will take another look at how this recession is different from the average recession in the postwar period. Here we will look at the four components of GNP -- consumers, businesses, foreigners, and government -- and calculate each sector's contribution to economic growth or, in this case, decline.

The table above shows the total real GNP decline to be 2.6 percent during the average recession and 1.1 percent during the projected recession, as discussed earlier. Summing the contributions of the four sectors gives the total growth rate. For example, the contraction in consumer activity during a typical recession causes the GNP growth rate to fall by 0.1 percentage points, as does the contraction in government purchases. Although these sectors together combine for almost 90 percent of the U.S. economy, the declines here are completely offset by an increase in international activity, which typically adds 0.2 percentage points to economic growth during a recession. The reduction in business spending, which usually takes away 2.6 percentage points of growth, can be said to account for the entire decrease in real GNP.

Contributions to Recession

(in percentage points)

	Average	Current
Consumers	-0.1	-0.9
Goods & Services	0.4	-0.6
Residential	-0.5	-0.3
Business	-2.6	-0.9
Plant & Equipment	-0.9	-0.5
Inventories	-1.7	-0.4
Government	-0.1	0.0
International	0.2	0.7
Total Real GNP	**-2.6%**	**-1.1%**

Note: This table breaks down the contribution made by each of the four components of GNP. For example, of the 2.6% total decline in GNP during the average recession, 0.1 percentage points can be attributed to consumers. Summing the contributions of the four sectors yields the total decline in GNP. This method goes beyond providing a simple percent change in each sector by taking account of each sector's relative importance in the economy.

The comparison of the average recession and the current recession demonstrates several points.

The Swing in Consumption Spending. While consumer spending on goods and services is typically reined in during a recession, it nevertheless still adds some strength to a recessionary economy, upping growth by 0.4 percentage points. But in the current recession, spending pulls growth down by 0.6 percentage points -- a full one percentage point swing in the contribution made to GNP growth. This demonstrates how much this is a consumer-led recession.

Inventories Stay Steady. As discussed earlier, inventories are playing a much more moderate role in this downturn. Business spending on inventories takes away 1.7 percentage points from GNP growth during the average recession. During the current recession, however, this will take only 0.4 percentage points from growth.

Bigger Role for Trade. The table illustrates another point made earlier: Exports will contribute importantly to cushioning this recession. Growth in trade will add an additional one-half of a percentage point to growth during the recession.

By Robert D. Barr
Director of Forecasting
Forecasting & Policy Analysis

U.S. Economic Outlook: January 1991

Quarterly figures are seasonally adjusted annual rates

	90.2	90.3	90.4	91.1	91.2	91.3	91.4	92.1	1988	1989	1990	1991	1992
U.S. Economy													
Annual Growth Rate													
Real GNP	0.4	1.4	-2.2	-1.5	-0.8	2.8	3.2	3.3	4.5	2.5	0.9	-0.2	2.9
Industrial Production	4.3	3.7	-7.4	-5.5	-2.2	2.5	4.1	3.6	5.4	2.6	1.0	-2.0	3.2
Civilian Employment	0.7	-1.5	-2.3	-0.9	-0.8	-0.0	0.8	1.3	2.3	2.0	0.4	-0.9	1.0
GNP Inflation Index	4.7	3.7	4.8	5.1	3.0	2.1	2.5	2.8	3.3	4.1	4.2	3.9	2.5
Consumer Prices	3.7	6.4	6.8	6.0	2.5	2.1	2.8	2.6	4.1	4.8	5.4	4.7	2.7
Value of the U.S. Dollar	-2.0	-20.7	-19.1	-5.2	0.2	4.3	0.3	-1.2	-4.3	6.2	-9.6	-7.6	0.2
Percent													
Mfg. Capacity Utilization	82.8	82.8	80.7	79.4	78.6	78.9	79.6	80.1	83.9	83.9	82.2	79.1	80.9
Civilian Unemployment	5.3	5.6	5.9	6.2	6.6	6.8	6.8	6.7	5.5	5.3	5.5	6.6	6.4
Percent of GNP													
Federal Tax Receipts	20.3	20.4	20.6	20.7	20.4	20.5	20.6	20.7	20.0	20.2	20.4	20.5	20.7
Federal Expenditures	23.4	23.1	23.4	23.7	23.8	23.7	23.5	23.5	22.9	22.8	23.3	23.7	23.3
Federal Budget Deficit	-3.0	-2.6	-2.8	-3.1	-3.4	-3.2	-2.9	-2.9	-2.9	-2.6	-2.9	-3.1	-2.6
Interest Rates, Percent													
Federal Funds Rate	8.2	8.2	7.6	6.8	6.6	6.6	6.9	7.2	7.6	9.2	8.1	6.7	7.3
3-Month T-Bill Rate	7.7	7.5	7.0	6.2	6.0	6.1	6.3	6.6	6.7	8.1	7.5	6.2	6.6
Prime Rate	10.0	10.0	10.0	9.6	9.4	9.0	9.0	9.0	9.3	10.9	10.0	9.3	9.0
Discount Rate	7.0	7.0	6.9	6.4	6.0	6.0	6.0	6.0	6.2	6.9	7.0	6.1	6.0
Corporate AAA Bond Yield	9.4	9.4	9.3	8.7	8.5	8.4	8.3	8.4	9.7	9.3	9.3	8.5	8.3
30-Year Government Bond Yield	8.7	8.8	8.5	8.0	7.8	7.7	7.7	7.7	9.0	8.4	8.6	7.8	7.7
Mortgage Rates, Percent													
30-Year Fixed Rate	10.3	10.1	10.0	9.5	9.2	9.0	9.0	9.0	10.3	10.3	10.1	9.2	9.0
1-Year Adjustable	8.6	8.4	8.1	7.9	7.8	7.7	7.5	7.5	8.5	9.3	8.3	7.7	7.5
Home Sales & Starts													
Thousands													
Total Single-Family Sales (Single-family resales plus 97% of single-family starts)	4,188	4,164	3,871	3,898	3,934	4,075	4,210	4,314	4,648	4,446	4,174	4,029	4,386
Existing Single-Family Sales	3,320	3,333	3,090	3,106	3,149	3,230	3,328	3,404	3,594	3,467	3,292	3,203	3,466
New Single-Family Sales	540	527	495	478	489	502	517	531	676	654	538	497	548
Housing Starts	1,204	1,130	1,052	1,022	1,029	1,118	1,179	1,224	1,491	1,386	1,210	1,087	1,248
Single-Family Units	895	857	805	816	809	871	910	939	1,086	1,010	910	852	948
Multi-Family Units	309	273	247	206	220	248	269	286	405	377	300	236	299
2-4 Family Units	44	31	28	23	25	28	31	32	59	55	37	27	34
5+ Family Units	265	242	219	182	195	220	238	253	347	321	264	209	265
Mobile Homes Shipped	190	187	187	192	183	193	200	202	218	199	190	192	204
Percent change -- Year Ago													
Total Single-Family Sales	-2.7	-5.5	-13.9	-12.9	-6.1	-2.2	8.8	10.7	0.4	-4.3	-6.1	-3.5	8.8
Existing Single-Family Sales	-0.6	-3.2	-12.6	-9.3	-5.1	-3.1	7.7	9.6	2.4	-3.6	-5.0	-2.7	8.2
New Single-Family Sales	-15.1	-24.7	-24.1	-19.3	-9.4	-4.7	4.4	11.1	0.8	-3.3	-17.6	-7.8	10.4
Housing Starts	-11.1	-15.5	-21.9	-29.8	-14.5	-1.0	12.1	19.9	-8.6	-7.0	-12.7	-10.2	14.8
Single-Family Units	-9.8	-13.9	-18.5	-24.7	-9.5	1.6	13.1	15.0	-5.9	-7.0	-9.9	-6.4	11.4
Multi-Family Units	-14.7	-20.2	-31.3	-44.6	-28.8	-9.3	8.9	39.0	-14.9	-7.1	-20.3	-21.5	27.1
2-4 Family Units	-18.1	-44.6	-47.5	-46.2	-42.8	-9.3	8.9	39.0	-10.0	-5.7	-34.1	-26.8	27.1
5+ Family Units	-14.1	-15.4	-28.5	-44.4	-26.4	-9.3	8.9	39.0	-15.7	-7.3	-17.9	-20.8	27.1
Median Home Prices													
Thousands of Dollars													
Existing Home Prices	96.2	96.6	92.1	92.4	93.7	94.8	96.7	99.1	89.2	92.9	95.2	94.4	100.5
New Home Prices	126.7	116.4	120.7	121.3	122.2	123.0	124.2	125.6	113.4	120.4	121.8	122.7	127.2
Percent Change - Year Ago													
Existing Home Prices	3.5	1.8	-0.6	-3.7	-2.6	-1.9	5.0	7.3	5.0	4.2	2.4	-0.9	6.4
New Home Prices	6.0	-2.7	-3.0	-1.5	-3.5	5.6	2.9	3.5	8.3	6.2	1.1	0.8	3.7

Source: Forecast produced using Laurence H. Meyer & Associates' model of the U.S. economy. Assumptions and simulations by Dr. John Tuccillo, Robert Barr and Kimberly Martin.